

SUBCOMMITTEE NO. 1 on Education



Subcommittee No. 1
Chair, Jack Scott
Member, Bob Margett
Member, Joe Simitian

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OUTCOMES

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ITEM 6110 DEPARTMENT OF EDUCATION**ISSUE 1: Financial Status of School Districts – Information Only**

DESCRIPTION: Presentation by Tom Henry, Chief Executive Officer and Joel Montero, Deputy Executive Officer, Fiscal Crisis & Management Assistance Team (FCMAT) on the financial status of school districts.

BACKGROUND:

Interim Financial Status Reports. Current law requires school districts and county offices of education (LEAs) to file two interim reports annually on their financial status with the California Department of Education. First interim reports are due to the state by January 15; second interim reports are due by April 15.

As a part of these reports, LEAs must certify whether they are able to meet their financial obligations. The certifications are classified as positive, qualified, or negative. A positive certification indicates that a LEA will meet its financial obligations for the current and two subsequent fiscal years; whereas a qualified certification indicates a LEA may not meet its financial obligations during this period. Under a negative certification, LEAs are unable to meet their financial obligations in the current year or in the subsequent fiscal year.

According to the First Interim Report for 2004-05 – the most recent report available – there are currently ten school districts with negative certifications and 50 school districts with qualified certifications. [See Appendix A for a complete list.] The ten school districts with negative certifications listed below will not be able to meet their financial obligations for 2004-2005 or 2005-2006.

District	County	Budget
Auburn Union Elementary	San Bernardino	\$17 million
East Side Union High	Santa Clara	\$204 million
Fresno Unified	Fresno	\$603 million
Hayward Unified	Alameda	\$175 million
Los Molinos Unified	Tehama	\$5 million
Oakland Unified	Alameda	\$425 million
Oro Grande Elementary	San Bernardino	\$1 million
Salinas City Elementary	Monterey	\$63 million
West Fresno Elementary	Fresno	\$8 million
Vallejo City Unified	Solano	\$146 million

Six districts have joined the latest negative status list – Auburn Union Elementary, East Side Union Elementary, Fresno Unified, Los Molinos Unified, Oro Grande Elementary, and Salinas City Elementary. Three other districts – Berkeley Unified, Corning Union Elementary, Livermore Valley Joint Unified – moved from the negative list to the qualified list.

Three school districts on the negative certification list – Oakland Unified, West Fresno Elementary and Vallejo Unified – have received emergency loans from the state. Two other school districts – West Contra Costa Unified and Emery Unified -- have emergency loans with the state, but are not on either the negative or qualified certification lists.

The numbers of school districts with negative and qualified certifications will reportedly increase when the Second Interim Report for 2004-05 is released by CDE later this spring.

Financial Pressures Facing School Districts. The LAO has identified four major financial pressures facing school districts that they will discuss at the subcommittee hearing today. These pressures include:

- (1) Lower revenues due to declining enrollment;
- (2) Restoration of state required reserves;
- (3) Restoration of operating balances; and
- (4) Higher costs for wage increases and health premiums/benefits.

The LAO will present proposals for addressing declining enrollment and health costs later in the subcommittee agenda.

Budget Flexibility Budget trailer bill language contained in AB 1754 (Chapter 227; Statutes of 2003) provided K-12 local education agencies (LEAs) with limited-term flexibility in accessing education reserves and balances of restricted funds in order to mitigate revenue limit reductions in the 2003-04 budget. Flexibility was provided in three general areas:

- Reduce minimum reserves for economic uncertainty to a range of .5 to 2.5 percent of budget (half the statutory level) in 2003-04 and 2004-05.
- Reduce school district maintenance reserves from 3 to 2 percent in 2003-04.
- Permit LEAs to access the 2002-03 ending balances for most categorical programs.

As indicated by LAO, restoration of statutory reserves and operating balances has created financial pressures for LEAs.

Control Section 12.40 of the budget gives LEAs additional budget flexibility allowing them to shift limited amounts of funding among categorical programs. This control section was added to the 1999-2000 budget to retain some of the transfer authority among categorical programs included in a budget “mega-item” that was eliminated that year. The original control section allowed transfer of up to 20 percent of funding out of any program and to transfer up to 25 percent into a program in the control section. The authority was lowered to 10 percent “out” and 15 percent “in” beginning in 2003-04 given the significant, limited-term budget flexibility provided to LEAs that year. The Governor’s 2005-06 budget continues this same level of flexibility for twelve categorical programs. (See Appendix B for list.)

QUESTIONS:

1. *Do you agree with the LAO's list of financial pressures facing school districts? What other factors are at play?*
2. *Chapter 52, Statutes of 2004 (AB 2756/Daucher) strengthens fiscal oversight of school districts, in particular county review and authority over school district budgets. Are county offices utilizing this new authority?*
3. *Are there additional reforms – beyond those contained in Chapter 52 – that the Legislature should consider to improve fiscal oversight of LEAs?*
4. *AB 1754 requires LEAs to report ending balance transfers – programs and amounts to the Superintendent of Public Instruction and the Joint Legislative Budget Committee in a timely manner. What do these reports tell us about the usefulness of ending balances in helping LEAs meet their budgets?*
5. *LEAs are required to report annually to the Department of Education on any amounts shifted between categorical programs pursuant to Control Section 12.40 of the budget. How would you assess the categorical funding transfers provided by Control Section 12.40?*

ISSUE 2: Declining Enrollment

DESCRIPTION: The LAO recommends that the Legislature address the financial pressures faced by many districts as a result of declining enrollment. An estimated 412 (42 percent) of school districts statewide are currently experiencing enrollment declines. Since school age population growth is predicted to decline further in the next five years, the number of declining enrollment districts is expected to climb. Current law allows districts to *delay* revenue limit reductions associated with enrollment declines for one year. The LAO proposes an *additional* option for districts. This option would *permanently increase* revenue limit funding for *most* declining enrollment districts whose revenue limits are below the statewide equalization target. Annual increases would be capped at five percent a year. Declining enrollment districts at the statewide target would continue to have the *one year* hold harmless provisions allowed under current law. The LAO also recommends consolidation of most revenue limit add-on programs within base revenue limits programs prior to any equalization.

BACKGROUND: The LAO's revenue limit proposal blends features that address both revenue limit equalization and declining enrollment, as well as, consolidation of revenue limit programs.

Declining Enrollment:

Data from the California Department of Education indicate that 412 school districts (42 percent) experienced declining enrollment in 2003-04. According to the LAO, additional data suggests that most of these districts also experienced declining enrollment.

According to the latest population estimates, the LAO predicts that statewide K-12 attendance growth will continue to fall over the next several years and by 2008-09 there will be no enrollment growth. For this reason, the LAO estimates that a large number of districts will continue to face declining enrollment. In addition, some of the 589 districts that are currently growing will start to decline.

The LAO reports most declining enrollment districts are small – reflecting the composition of districts statewide. However, 35 districts have more than 10,000 students (and of these 12 have more than 25,000 or 50,000 students). Approximately 27 percent of the state's students attend declining enrollment districts. The average enrollment loss to school districts is 1.7 percent; but one-quarter of districts reported declines of more than 5 percent.

On face, declining enrollments translate into declining costs to school districts (i.e. fewer students, fewer teachers, etc.). However, districts don't save as much in costs as they lose in revenues. At the most basic level, when districts reduce their teaching force, they reduce their less experienced, lower paid teachers.

Equalization:

The LAO estimates that most declining enrollment districts have revenue limits that are below the state equalization target set at the 90th percentile of districts of different size (small and large)

and types (elementary, high, unified). Reportedly, most districts are within 10 percent of this target. The LAO estimates the cost of bringing all declining enrollment districts to the 90th percentile at approximately \$130 million, and the cost of bringing school district revenue limits in the state to the 90th percentile is estimated at around \$450 million.

Consolidation:

In addition to base revenue limits, there are nine adjustments or revenue limit add-on programs. Base revenue limits account for 95 percent of revenue limit funding; revenue limit add-on programs – totaling nearly \$1.6 billion annually account for the remaining 5 percent. Revenue limit add-on programs include: teacher salary incentive program; the Unemployment Insurance program; PERS offset; longer school days and year incentives; Meals for Needy Pupils, etc. Since revenue limit add-on programs are allocated very unevenly among districts, they contribute to revenue limit funding inequities among school districts. However, they are not included in revenue limit equalization calculations. For this reason, the LAO recommends that five revenue limit add-on programs be consolidated into base revenue limits to more accurately equalize general purpose funding among school districts.

Governor's Budget: The Governor's Budget does not address the issue of declining enrollment directly, but does propose \$329 million in revenue limit deficit factor payments in 2005-06. The 2004-05 budget package appropriates \$110 million for K-12 revenue limit equalization funding for school districts (not county offices), setting the target at the 90th percentile of districts within each size and type. The Governor does not propose additional funding for equalization in 2005-06.

Costs of LAO Proposal: There are no budget year costs with the LAO's proposal. However, there would be additional costs of approximately \$25 to \$60 million per year in 2006-07 for equalization payments to eligible declining enrollment districts. This cost would increase over time as districts take advantage of this option each year. Annual costs will depend upon the number of districts that opt for the proposed adjustment instead of the one year hold harmless provision allowed under current law. The estimated cost of equalizing revenue limits for *all* school districts in the state in approximately \$450 million.

Legislation: Several bills that address equalization and declining enrollment have been introduced this session, including:

- **SB 958 (Simitian)** – Allows declining enrollment districts to calculate revenue limit funding using the average ADA over a two period, if they have been in decline for two years, or over a three year period if they have been in decline for three years or more.
- **AB 1503 (Mullin)** - Allows declining enrollment districts to claim 60 percent of the difference between ADA in the year prior to the first year of decline and ADA in subsequent years of decline.
- **AB 60 (Nunez)** - Revises computation factors of revenue limit equalization adjustment to be based on: a) enrollment instead of ADA; b) elementary, high school, and unified districts without respect to size; c) all unrestricted funding, not just base revenue limits.

COMMENTS/RECOMMENDATIONS: Staff believes that the LAO's proposal has merit, but has significant out year costs at a time when schools face other significant, outstanding funding obligations. However, the Subcommittee may wish to study the LAO's proposal further as a possible option for using additional funding beyond growth and COLA in future years. Funding for this purpose would have to be weighed against other funding priorities the Subcommittee has already discussed including revenue limit deficit factor and education mandate payments, with the caveat that decisions would affect costs in the 2006-07 fiscal year.

QUESTIONS:

1. *While the LAO has recommended that the Legislature make progress in equalizing revenue limits in recent years, last year the LAO recommended against any funding for revenue limit equalization until a year when Proposition 98 "credit card obligations" – revenue limit deficits, unfunded state mandates, and payment deferrals -- could be paid off? How does the LAO's current proposal stack up to these other competing priorities?*
2. *Without supplemental funding for equalization, how long would it take to equalize funding for school districts to the 90th percentile target?*
3. *What is the effect of declining enrollment on different types of school districts and does the LAO's proposal recognize these differences?*

OUTCOME: No action.

ISSUE 3: District Health Benefit Liabilities

DESCRIPTION: The LAO raises concerns about large *and growing* retiree health benefit liabilities that are creating significant fiscal pressures for some school districts in the state. In response, the LAO recommends enactment of legislation to: require districts to report their retiree benefit liabilities to county offices of education (COEs) and develop plans for addressing these liabilities; require COE's to include the review of long-term health benefit liabilities as a part of their district fiscal oversight responsibilities; and require CDE to report to the Legislature on the size of retiree health liabilities for 150 school districts with the most extensive benefits.

BACKGROUND:

School districts provide retirement pension, health and other benefits to their employees. According to the LAO, while school districts pre-fund retirement pensions for their employees through annual contributions, they do not reportedly pre-fund health insurance benefits. Instead, they pay for benefits directly through their operating budgets once the benefits are claimed by retirees. This situation creates future liabilities for school districts when these retirement costs come due. Until recently, the significant size of these liabilities in some districts was not known statewide.

In the past, the state has mandated that school districts conduct an actuarial study of their retiree benefits. The LAO reports that new Government Accounting Standards Board (GASB) policies require school districts to account and report its long-term retirement liabilities in their annual financial statements. These new requirements have brought new attention and concern to the issue of large and growing district health insurance retirement liabilities.

Per the LAO, Fresno Unified has an unfunded liability for retiree health benefits of \$1.1 billion, which equates to more than twice its general purpose operating budget. Fresno Unified currently has a negative fiscal certification on the state's fiscal status list. Los Angeles Unified has an unfunded health benefit liability of \$5 billion, which equates to 80 percent of its operating budget. The LAO notes that using other reasonable assumptions, Los Angeles Unified's liability climbs to \$11 billion.

The LAO indicates that new GASB policies encourage, but do not require, school districts to pre-fund all their retirement benefits. According to the LAO, Los Angeles is currently spending \$170 million a year for retiree health benefits. It would cost Los Angeles an additional \$500 million (8 percent of its budget) in 2005-06 to pre-fund benefits for existing employees and cover its unfunded liabilities.

LAO Recommendation:

The LAO is concerned about the significant size of retiree health benefit liabilities for school districts. Without immediate action, the LAO is concerned that these liabilities will translate into fiscal crisis in some districts that will require state bail out. The LAO is further concerned

that school districts may lack incentives for addressing or curbing these costs without outside intervention. For this reason, the LAO recommends the Legislature enact legislation to:

- Require districts to provide COEs, by October 1, 2005, with a copy of any actuarial study of its retiree benefits liability.
- Require districts to provide COEs, by June 30, 2006, with a plan for addressing retiree benefits liabilities.
- Modify AB 1200 to require COEs to review whether districts' funding of long-term liabilities adequately cover likely costs.
- Require CDE to report to the fiscal committees of the Legislature by December 15, 2005 on the size of retiree health liabilities in the 150 districts that provide the most extensive benefits.

RECOMMENDATION: Subcommittee members became aware of the fiscal pressures of rising health insurance costs for school districts as a result of testimony provided at their three regional town hall meetings held in February 2005. These town hall meetings were held in Fresno, Salinas, and San Diego.

Given large and growing liabilities reported in Fresno Unified and other districts highlighted by the LAO, *staff recommends* that the Subcommittee adopt the LAO's recommendations. It appears that the size and scope of retiree health benefit liabilities have been somewhat hidden until recently. The LAO's recommendations to formalize reporting and review of these expenditures at the state and local level are very reasonable steps for developing a better understanding of this issue and for controlling these costs through improved fiscal oversight by COEs.

Staff notes that there may be additional costs associated with placing new responsibilities on districts, COEs and CDE as recommended by the LAO. On the other hand, these responsibilities might fall within the realm of the existing review responsibilities for COEs. *Staff recommends* that the Subcommittee clarify these costs at the hearing.

OUTCOME: No action. Subcommittee requested that the LAO look into the issue of Medicare coordination.

ISSUE 4: Federal Funds Overview – Information Only

DESCRIPTION: The Governor's Budget estimates that California will receive \$7.5 billion in federal funds for K-12 education in 2005-06, which represents a decrease of \$51 million (0.7 percent) in the budget year. The Department of Finance will update its federal fund estimates at May Revise to reflect the latest figures from the federal government. According to the Department of Education, the Governor's Budget underestimates federal funds appropriated through the California Department of Education by \$125 million in 2005-06, and as a result federal funding overall should actually increase by \$75 million in 2005-06.

BACKGROUND: Of the \$7.5 billion in federal funds proposed in the Governor's Budget, \$6.9 billion is appropriated through the California State Department of Education (CDE). Approximately \$600 million in additional federal grant funds are appropriated directly to local school districts or schools.

The \$6.9 billion in federal funds for CDE in the Governor's Budget is appropriated from three major federal agencies – the U.S. Department of Education, U.S. Department of Health and Human Services, and the U.S. Department of Agriculture. Four specific federal programs – child nutrition (school meals); Title I (compensatory education); child development (child care); and special education – provide the most federal funding to K-12 schools in California. These four programs are among the largest federal programs -- of any type -- to our state.

The table below reflects federal funds for these and other programs included in the Governor's Budget for 2005-06. Figures are based upon appropriations for federal fiscal year (FFY) 2005.

Federal Funds -- Agency/Program	FFY 2005
<i>US Dept. of Education:</i>	
Title I and Other Programs Authorized Under NCLB	\$3,001,295,000
Special Education – IDEA	1,153,212,000
Vocational & Adult Education, Tech. Prep. Education – Perkins & WIA	218,366,000
Subtotal, USDE Funds	\$4,372,873,000
<i>US Dept of Agriculture:</i>	
School Nutrition – School Lunch, Breakfast, Summer Meal Programs	\$1,616,804,000
Subtotal, USDA Funds	\$1,616,804,000
<i>US Dept of Health & Human Services:</i>	
Child Care – TANF & Child Care and Development Block Grant	\$934,042,000
Subtotal, USHHS Funds	\$934,042,000
Total, Federal K-12 Education Grants to California	\$6,923,709,000

The Department of Finance plans to update these figures at May Revise to levels contained in Labor/HHS/Education appropriations bill signed by the President in December 2004 as a part of the FFY 2005 omnibus budget package. It is anticipated that federal funding levels will increase by another \$125 million translating into an overall increase of \$75 million (1.0 percent), rather than a decrease of \$51 million (0.7 percent) estimated in the Governor's January 10 budget.

The one percent increase in federal funds to California is significantly lower than federal increases in the last several years. Between FFY 2001 and FFY 2004, federal funding to California for elementary and secondary education programs grew between 8 and 12 percent. (See Appendix C for latest federal estimates of USDE formula grants to California for FFY 2005.)

The FFY 2005 budget includes a 0.80 percent across-the-board reduction for agencies and programs, which provides some explanation for lower federal funds. In addition to somewhat flat funding for most programs, federal appropriations for FFY 2005 include *reductions* to several specific programs. For federal programs that flow through CDE, some reductions include Education Technology State Grants (\$27.8 m) and school improvement funding from for State Grants for Innovative Programs (\$12.1 m). In contrast, two of the largest federal programs received *some* increases – Title I Basic Grants for Disadvantaged Students (\$16.9 m) and Special Education (\$59.9 m). Year-to-year changes in federal grants to California that flow through CDE are listed below.

Federal Grants to California That Flow Through CDE *

Budget Item 6110-	Program	FFY 2004	FFY 2005	Change
102-0890	Learn and Serve America	2,339,000	2,690,544	351,544
103-0890	Byrd Honors Scholarship	5,166,000	5,139,000	-27,000
112-0890	Charter Schools	37,822,000	25,107,664	12,774,336
113-0890	State Assessments	32,267,812	33,527,053	1,259,241
119-0890	Title I (Part D) - Neglected and Delinquent	3,249,282	3,240,296	-8,986
123-0890	Title I- Comprehensive School Reform	31,344,563	27,680,353	-3,664,210
	Title V – Innovative Programs	36,429,854	24,372,684	-12,057,170
125-0890	Title III - Migrant Education	127,573,296	126,526,065	-1,047,231
	Title III – Language Acquisition Grants	161,549,115	155,390,437	-6,158,678
126-0890	Title I (Part B) - Reading First Grants	146,145,963	146,981,710	-835,747
136-0890	Title I (Part A) – Basic Grants	1,694,916,121	1,711,604,862	16,688,741
136-0890	Title I - School Support Set Aside	70,621,505	71,316,869	695,364
136-0890	Even Start	31,451,159	27,810,338	-3,640,821
136-0890	Homeless Education	8,500,225	8,644,457	144,232
137-0890	Rural/Low-Income School Program	1,425,730	1,449,457	23,727
156-0890	Adult Education	82,338,152	81,473,634	-864,518
161-0890	Special Education-Entitlement Grants	1,072,636,899	1,132,572,659	59,935,760
	Special Education-Preschool	39,550,707	39,160,720	-389,987
166-0890	Vocational Education	140,027,486	140,277,947	461
180-0890	Education Technology	93,318,376	65,555,871	-27,762,505
183-0890	Safe and Drug Free Schools	53,257,421	52,742,911	-514,510
193-0890	Title II (Part A) Math & Science Partnerships	20,616,756	24,513,072	3,896,316
195-0890	Title II (Part A) – Teacher Quality Grants	341,331,785	339,015,227	-2,316,558
197-0890	21st Century Community Learning	136,981,161	137,174,714	193,553

**Please note: These figures are actual and estimated figures from USDE and will not exactly match budgeted amounts due to carryover funds and funds scheduled in state operations items.*

COMMENTS: *Staff notes* that new federal funds in recent years have been critical to underwriting important programs of interest to the Legislature, for example accountability programs to assist low-performing schools, state assessment programs, after-school programs, early reading programs, programs to support English learners, and special education. While the state has a strong interest in maximizing these funds, several programs – 21st Century Learning Centers, Migrant Education, Title I – Set Aside, Title VI –Assessment, and Reading First have been troubled by large and growing carryover balances. Federal funds remain available for 27 months after appropriation. However, it has been difficult for some of these programs to expend funds within this time period. If not addressed, the state could lose these valuable federal funds. The Subcommittee will consider these issues for specific programs at the hearing today and future hearings.

QUESTION:

1. *How can the Legislature better spend federal funding to avoid large carryover balances?*
2. *What are the challenges of appropriating and expending carryover balances?*
3. *What information does CDE have about future federal funding for California?*

ISSUE 5: Special Education – Allocation of Federal Funds

DESCRIPTION: The Governor’s Budget and LAO have developed different proposals for allocating approximately \$62 million in additional federal special education funds in 2005-06. The Governor’s plan gives priority to increasing grants to LEAs and expanding funds for the new LCI formula. The LAO’s plan gives priority to funding mental health related services. Current state law requires that federal funding be used to offset to state growth and COLA expenditures. New federal law now prohibits this practice in states.

BACKGROUND: The Governor’s Budget proposes \$4.3 billion in special education funding in 2005-06. Of this amount, the budget includes **\$1.1 billion** in federal special education funds for students ages 3-21 years in 2005-06. This reflects an increase of \$64.7 million in the budget year. Federal funds account for approximately 25.5 percent of the funds in the state special education budget; when accounting for all special education funding, including local funds, the federal share is less. Federal funds are authorized under Part B of the Individuals with Disabilities Act (IDEA).

The Governor's Budget also proposes **\$2.9 billion** in General Fund support (Proposition 98) and **\$347.9 million** in property taxes for special education in 2005-06. The table below displays special education funding for 2004-05 and 2005-06.

<i>Dollars in Millions</i>	2004-05	2005-06	Dollar Change	Percent Change
General Fund	\$2,756.7	\$2,891.3	\$134.6	4.9 %
Property Taxes	332.6	347.9	15.3	4.6 %
Federal Funds	1,046.2	1,110.9	64.7	6.2 %
TOTALS	\$4,135.5	\$4,350.1	\$214.6	5.1 %

Funding Changes Pursuant to 2004 IDEA Reauthorization:

As signed into law in December 2004, the newly reauthorized IDEA includes changes affecting special education funding to states. Most importantly to California, the new federal law prohibits states from using federal funds to offset state mandated funding obligations, including program growth and cost-of-living adjustments (COLAs).

Under current law, the state uses federal funds to offset state growth and COLA payments. While this is not the practice for most other states, California has utilized this practice for more than 25 years, except for a few years following implementation of the AB 602 funding formula in 1997-98. During these years, the offset was placed on hold in order to provide additional resources to equalize special education funding among SELPAs to the statewide target. In the current year, the state used \$124 million to offset special education growth and COLA.

The new federal law continues to “authorize”, not entitle or guarantee, federal special education funding up to 40 percent of the average state expenditures for special education. States currently receive approximately 20 percent or half of the funding authorized. Federal funding to

California would roughly double if states received funding at the 40 percent (“fully authorized”) level.

The new federal law does include a schedule for increasing IDEA funding to the 40 percent level. However, while the IDEA authorizes funding it does not appropriate funds. The President’s education budget for FFY 2006 currently proposes funding below the levels scheduled in the reauthorized IDEA.

Allocation of Federal Funding Increase:

The Governor’s budget appropriates approximately \$62.2 million in new federal funds for special education local assistance in 2005-06. The Governor proposes to expend these funds as follows: \$38.1 million to increase the federal contribution of federally mandated special education services pursuant to AB 602, including \$20.2 million to increase funding for the new Out-of-Home-Care funding formula and \$17.2 million for other baseline increases; as well as \$24.8 million as a pass-through for special education formula grant increases to LEAs.

The LAO recommends an alternative expenditure plan for the new federal funds. The LAO proposes to use the \$62.2 million in federal funds as follows: \$42.8 million to support mental health related services for special education students; \$2.2 million as a technical adjustment to add a small number of resident counts (budget year) to the new LCI (Licensed Children’s Institution) formula; and \$17.9 million for other purposes.

In addition, the LAO has identified another \$26.6 million in one-time, special education savings in a prior year that must be used for special education purposes. The LAO proposes to use \$2.2 million to add resident counts (current year) to the LCI formula and use the remaining funds as a one-time block grant to LEAs.

The Governor’s Budget utilizes \$38.1 million to offset federal funds; however, the Administration reports they do not offset General Fund growth and COLA expenditures in a manner that might be prohibited by the federal law. The LAO recommends that the Legislature separate state and federal funding for budgeting purposes and use federal funds to pay for growth and COLA for federal programs. According to the LAO, this would comply with the supplanting provisions of the new federal law.

RECOMMENATIONS/COMMENTS: *Staff recommends* that the Subcommittee delay action on special education items until after May Revise. The LAO has presented several options for the Legislature to consider during this time. It is also very likely that the Administration will update their proposal at that time. It is important to point out that the reauthorized IDEA was not signed into law until December 2004, so there was not much time for the Administration to interpret and integrate new funding requirements in the budget.

The three following agenda items provide additional detail on several of the individual program proposals summarized in this item.

OUTCOME: **No action.**

ISSUE 6: Mental Health Related Services

DESCRIPTION: The Governor's Budget recommends suspending AB 3632 mandates on counties and shifting responsibility for mental health related services to education. This would require legislation that would be worked out in various policy committees. The LAO also recommends shifting responsibility for mental health services to schools, but on a permanent basis. The LAO also recommends providing \$42.8 million in additional funds to LEAs to provide these needed services.

BACKGROUND: The Governor's Budget recommends suspending two mandates that require counties to provide mental health related services to special education students. State legislation passed in the mid-1980s – AB 3632 -- shifted responsibility for mental health related services from the schools to counties, and created a reimbursable state mandate as a result.

While AB 3632 shifted responsibility to counties, mental health related services for students with disabilities are specifically mandated under federal special education law. State and local education agencies are ultimately responsible for assuring the provision of these services to students with disabilities under federal law.

The Governor's 2005-06 budget proposes to continue current year funding of \$100 million for mental health related services for students with disabilities in the K-12 budget. This amount includes \$69 million in federal funds to reimburse counties for AB 3632 services and \$31 million in General Funds for mental health pre-referral services provided by SELPAs (Special Education Local Planning Areas).

The Governor does not propose any county funding for mental health related services. In addition, the Governor's proposed suspension would appear to eliminate any requirement on counties for providing these services under the provisions of Proposition 1A, which was passed by voters last November. Under this scenario, counties could not claim reimbursements for AB 3632 services.

LAO Proposal: The LAO recommends permanently assigning responsibility for mental health related services to SELPAs. According to the LAO, shifting responsibility to schools would result in a more effective and efficient delivery of services. Under the current mandate reimbursement system, counties have an incentive to inflate costs. In addition, since SELPAs can refer students to counties they have no incentives for providing early intervention services that could reduce the need for more costly and intensive services.

Under the LAO's model, SELPAs could provide services either directly or indirectly through counties. SELPAs currently contract out for many special education services, most notably with non-public schools and agencies. SELPAs could continue to collaborate with county mental health agencies in the delivery of services in order to meet student needs in the most effective and efficient manner.

According to the LAO, the annual cost of providing mental health related services under AB 3632 totals \$143 million. The LAO has identified \$143 million in special education funds within the K-12 budget to cover these costs in 2005-06. Specifically, the LAO utilizes the \$100 million in existing education funds continued by the Governor and recommends the addition of \$43 million from new funds available for special education in 2005-06.

The LAO further recommends all of the \$100 million in existing special education funds be rolled into the base to give SELPAs more flexibility for providing services. Currently, the \$69 million is allocated to county offices of education to transfer to county mental health, which does not provide options for school districts to provide services directly if they choose. The remaining \$31 million is available for early mental health services intended to prevent the need for more intensive and costly services.

SB 1895 Report: As enacted, SB 1895 (Burton) requires the Superintendent of Public Instruction to submit a report to the Legislature by April 1, 2005, that includes specific information and recommendations relating to the provision and monitoring of mental health related services. The report was not available in time for this agenda; however, CDE will provide the report to the Subcommittee at the April 4th hearing and summarize their findings and recommendations.

COMMENTS/RECOMMENDATIONS: *Staff recommends that the Subcommittee delay any action on mental health related services until after May Revise.* The Administration's proposal has opened up discussion about how to fund and provide mental health related services to students with disabilities.

Staff notes that the LAO has identified some additional education funds available in 2005-06 that the Subcommittee could provide for these services. *Staff also notes*, that if responsibility was assigned to schools, the SELPAs would need additional flexibility in utilizing funds for service delivery, as recommended by the LAO. In this way, SELPAs could choose to provide services or continue to contract with county mental health agencies for services. *Staff further notes* that in order to assure the continuation of high quality services for students with disabilities, the Subcommittee could consider establishing independent monitoring of services and augmenting statewide training for the transition period, at least. Training should reflect research and best practice and could also reflect model programs that involve effective collaboration between schools and county mental health agencies.

OUTCOME: **No action.**

**ISSUE 7: Special Education – Licensed Children’s Institutions (LCI)
Formula Adjustments**

DESCRIPTION: The Governor’s Budget proposes to increase funding for the LCI formula by \$20.2 million. The LAO favors other expenditure options at this time, but recommends technical adjustments to the LCI formula to recognize residents of community care facilities. Adding counts for these residents would increase ongoing funding by \$2.2 million. The Subcommittee may wish to consider options for changing the base year for the LCI formula from 2002-03 to 2003-04 to reflect more up-to-date expenditures for SELPAs. The base year has importance for determining the hold harmless levels for SELPAs under the formula.

BACKGROUND:

Governor’s Proposal to Increase LCI Formula Funding: The Governor’s Budget proposes an augmentation of \$20.2 million to increase funding for the new LCI funding formula. This augmentation would provide a second installment of funds, bringing total funding to \$187.9 million in 2005-06. The 2004-05 budget provided an initial augmentation of \$34.8 million. Full funding of the program, under the model established by the AIR study, would cost over \$205 million.

LAO Proposal to Make Technical Adjustment to LCI Counts: The LAO recommends that the Legislature adopt trailer bill language to change the statute establishing the new Licensed Children’s Institutions (LCI) funding formula in order to recognize residents of community care facilities. These residents were unintentionally left out of the LCI counts utilized by the new formula. This proposal would increase costs by \$4.4 million -- \$2.2 million in the current year and \$2.2 million in the budget year. The LAO recommends using one-time special education funds to pay for the current year adjustment and using federal funds to pay for the ongoing costs of adjustment.

Changes to the Base Year: The new LCI formula, as contained in statutory provisions contained in the budget trailer bill last year (SB 1108), contain hold harmless provisions for SELPAs. Under these provisions, SELPAs that are predicted to lose funding under the new formula, would be held harmless for two years for reductions below their 2002-03 reimbursement funding level. After two years, SELPA funding ratchets down to the new formula levels over a five year period.

Due to concerns about irregular and possibly inflated reimbursement claims from SELPAs in 2003-04, there was consensus for using 2002-03 as the base year for establishing hold harmless levels. According to CDE, irregularities in the 2003-04 data have now been corrected. For this reason, there is interest among SELPAs for changing the base year from 2002-03 to 2003-04. The purpose of these requests is to increase the level of hold harmless funding for SELPAs.

It is not yet known what a change in the base year would mean for all SELPAs. CDE has recently certified reimbursements for both 2002-03 and 2003-04. Reimbursements to SELPAs increase by more than \$10 million during this time. However, claims did not uniformly increase

for all SELPAs. It is also not known how these changes affect new estimates of winners and losers that will be developed by CDE during the month of April.

If the base year is changed, it would increase the amount of funding going to hold harmless SELPAs and decrease new funding for SELPAs that are winners under the new formula, unless new funding is provided.

RECOMMENDATIONS: *Staff recommends* that the Subcommittee request that the LAO and CDE (1) review certified reimbursement claims for 2002-03 and 2003-04, together with the April formula counts for 2004-05, and (2) develop options for updating the base year formula. *Staff recommends* that LAO and CDE provide options to the Subcommittee at May Revise.

Staff recommends that the Subcommittee delay action on all other issues in this item until after May Revise when the Subcommittee takes actions on other special education items. At that time, staff recommends that the Subcommittee approve of the LAO recommendation to adopt budget trailer bill language to add community care facility counts for youth to the LCI formula. At that time, *staff also recommends* that if such funds are not needed for maintaining mental health related services, the Subcommittee give high priority to providing additional funding for the LCI formula, as recommended by the Governor.

OUTCOME: No action. Subcommittee requested LAO and CDE to develop data and options for changing the LCI base year formula that would be available at May Revise.

ISSUE 8: Special Education – Special Disability Adjustment

DESCRIPTION: The LAO recommends that CDE report to the Subcommittee on the costs and feasibility of having the department assume responsibility for annual recalculation of the special incidence adjustment.

BACKGROUND: The incidence adjustment is a calculation that is included as a part of the AB 602 funding formula in order to account for students with high cost, low incidence disabilities. When AB 602 funding reforms were enacted in the late 1990s, the funding model changed from a model based upon the number of special education students to a model based upon the general school population. At that time, there was concern that the new model would not recognize the high costs for some special education students. To address that issue, AB 602 required a study to recommend a low incidence, high cost disability adjustment.

The resulting study, published by the American Institutes of Research (AIR) in 1998, recommended the creation of the incidence factor that was added to the AB 602 funding formula. That same study recommended that the formula be updated every five years. As a result, the Legislature funded another study, published by AIR in 2003.

The latest AIR study is intended to update the adjustments now in place. The recommendations would make substantial changes to definitions, costs, and allocations for the incidence adjustments now in place among SELPAs. In addition, the recommended revisions to the incidence adjustment interact with the recommended LCI formula in ways that are not well understood.

RECOMMENDATIONS: *Staff recommends* that the Subcommittee have CDE report at this hearing on the feasibility of conducting a recalculation of the special incidence formula. *Staff further recommends* that the Subcommittee request that LAO and CDE assess the impact of implementing the AIR recommendation for SELPAs and develop implementation alternatives for the Subcommittee to consider at its May 2nd hearing.

Staff notes that because the existing incidence adjustment expires at the end of the fiscal year, budget bill language is needed to continue the existing formula in the budget year.

OUTCOME: **No action. Subcommittee requested LAO and CDE to assess the impact of implementing the AIR recommendations and developing implementation alternatives for consideration at the May 2nd hearing.**

ISSUE 9: Assessment

DESCRIPTION: The Governor's Budget proposes to continue state General Fund and federal funds for state assessment with small changes in 2005-06.

BACKGROUND:

Governor's Budget. The Governor's Budget proposes expenditures of \$117.1 million for development and administration of student assessments statewide in 2005-06. Of this amount, the budget proposes expenditure of \$85.7 million in General Funds and \$31.3 million in federal Title VI funds. The following table summarizes assessment expenditures proposed by the Governor in 2005-06.

Governor's Budget – Student Assessment	General Fund	Federal Funds – Title VI	Total
STAR Program	\$63,946,000	\$2,180,000	\$66,126,000
STAR Test Development	1,407,000	535,000	1,942,000
CELDT Assessment	11,437,000		11,437,000
CELDT Assessment		10,156,000	10,156,000
CELDT Vertical Scaling Project		300,000	300,000
High School Exit Exam	6,761,000	8,121,000	14,882
High School Exit Exam Workbooks		2,500,000	2,500,000
High School Exit Exam: Evaluation of Instruction		261,000	261,000
Primary Language Test Development		3,000,000	3,000,000
California Alternate Performance Assessment		2,200,000	2,200,000
Alternative Schools Accountability Model		775,000	775,000
Assessment Reporting and Review	2,313,000	600,000	2,913,000
NCLB AYP Reporting		650,000	650,000
California High School Proficiency Exam	1,020,000		1,020,000
Reimbursements	-1,020,000		-1,020,000
	\$85,864,000	\$31,278,000	\$117,142,000

The Governor proposes two small changes to assessments in 2005-06. The Governor proposes a General Fund increase of \$5.6 million for assessment programs to replace one-time federal funding available in 2004-05. In addition, the Governor proposes \$4.5 million in additional funding as a baseline adjustment to reflect workload factors.

Federal Title VI Funds. Federal Title VI funds for State Assessments provide states with funds to help cover the costs of meeting the assessment and data requirements of NCLB, including developing or improving assessments, developing curriculum and performance standards, expanding testing accommodations for English learners and students with disabilities, developing student data systems to track achievement and other indicators – *such as graduation rates* – required by No Child Left Behind (NCLB), and increasing local capacity for improving student achievement.

RECOMMENDATIONS: *Staff recommends* that the Subcommittee approve this item after May Revise when Governor revises estimates for federal Title VI funds. *Staff further recommends* that the Subcommittee consider budget bill language directing the balance of any

unused Title VI funds available in 2005-06 (and any carryover funds from previous years) to expedite development of student graduation rates required by NCLB.

OUTCOME: No action.

ISSUE 10: Accountability

DESCRIPTION: The Governor's 2005-06 budget proposes to continue funding for several federal accountability grant programs reflecting allocation levels and patterns in the current year budget, absent one-time carryover funds. However, new requirements under the No Child Left Behind Act (NCLB) facing California may require the Legislature to revisit the allocation of federal accountability funds in the budget year. Most notably, the recent identification of 150 new school districts in our state requiring program improvement may require additional funding or at the very least a reallocation of funding as currently proposed. In addition, there have been problems with expending federal accountability funds in a timely fashion. This has resulted in the accumulation of excess carryover funds for some federal programs, specifically Title I – Set Aside funds for school improvement.

BACKGROUND:

Governor's Budget: The Governor's Budget proposes to expend \$339.7 million for accountability programs for underperforming schools in 2005-06. Of this amount, \$93.5 million (36 percent) is federal funding and \$246.2 (64 percent) is state General Fund. Most of this funding is utilized to provide limited-term, school improvement grants to low-performing schools and districts. Funding for specific state- and federally-funded accountability programs, as proposed by the Governor's 2005-06 budget, is summarized in the table below.

Item: 6610-	Program	Federal Funds	State General Fund	Total , All Funds
123	School Grants -- II/USP Program (\$200/pupil)	0	\$7,519,000	\$7,519,000
123	School Grants – High Priority (HP) Schools Program (\$400/pupil)	0	238,689,000	238,689,000
123	School Grants - Program Improvement and other Schools (\$200/pupil)	40,078,000 (Title I- School Reform)	0	40,078,000
136	State System of School Support Team for Program Improvement Schools/Districts	\$10,000,000 (Title I- Set Aside)	0	10,000,000
136	School Assistance & Intervention Teams (for II/USP and HP Schools)	8,600,000 (Title I- Set Aside)	0	8,600,000
136	District/School Grants: Assessment funds for Program Improvement or At-Risk Districts (\$10,000/school; \$50,000/district)	34,809,000 (Title I- Set Aside)	0	34,809,000
136	School Grants – Funding for Implementation of Corrective Actions (\$150/pupil)	13,600,000 (Title I- Set Aside)	0	13,600,000
	Total, All Programs	\$93,487,000	\$246,208,000	\$339,695,000

California maintains two different, but related accountability systems – one state and one federal -- that provide assistance and define sanctions for low-performing schools and districts.

State General Funds are utilized exclusively for state programs. Most funding is provided for the state's High Priority (HP) Schools program, which provides intervention grants to schools in Deciles 1 and 2 of the Academic Performance Index (API). There are currently 659 schools participating in the HP program. State funding for the Intermediate Intervention/Underperforming Schools (II/USP) program, targeted to schools in Deciles 1 -5 of the API is

minimal. In 2005-06, the state will make a final deferral payment for activities conducted in the current year for the third and final cohort of the II/USP program. Greater priority has been given to the HP program, which focuses resources on the state's lowest performing schools.

Federal funds are utilized for a variety of different improvement grants for both schools and districts that have been identified as needing program improvement under the No Child Left Behind Act (NCLB). Federal funds are also used for sanctions for schools and districts in the state and federal programs that have failed to make improvements. There are currently 1,626 schools and 150 districts that have been deemed as needing program improvement.

Federal funds are also utilized for both state and federal program sanctions. To date, sanctions have involved the assignment of independent intervention teams to schools that are not making progress. State System of School Support Teams are utilized for Program Improvement (PI) schools and districts under NCLB, whereas, School Assistance and Intervention Teams are utilized for HP and II/USP schools.

There are two sources of federal accountability funding that are available to states for improvement of low-performing schools including: Title I – Part A Set-Aside Funds and Title I – Comprehensive School Reform Grants.

Allocation of Title I –Set Aside Funds

Federal law requires that states set-aside four percent of their Title I -Part A grant funds for school improvement purposes. Prior to 2004-05, states were required to set-aside two percent of their Title I grants. These funds are to be used to assist schools and districts identified for program improvement.

On March 8, 2005 Superintendent of Public Instruction announced an agreement with the US Department of Education on changing the criteria for identifying program improvement (PI) districts. USDE had earlier challenged California's criteria for failing to comply with NCLB. As a result of this agreement, CDE has designated 150 PI districts. The CDE and DOF are currently discussing whether to provide funding for these districts in the current year. This development may also require a fundamental rethinking of the Governor's 2005-06 budget as it relates to the allocation of federal Title I – Set- Aside funding for program improvement in particular. The Governor's Budget proposes \$38.4 million in Title I – Set-Aside funds for districts in program improvement.

In total, the Governor's Budget provides \$67.0 million in federal Title I –Set Aside funds in 2005-06. This figure is likely to increase to approximately \$71 million at May Revise to reflect more recent federal Title I estimates for FFY 2005. Depending upon how CDE and DOF resolve the current year funding for districts in program improvement, there may be carryover from the current year.

Last year, there was concern that the state had not expended enough of its Title I Set-Aside funds in the previous two years, and that the state had accumulated large carryover balances that would

need to be spent in 2004-05 and 2005-06 in order to avoid reversion. The 2004-05 budget contained more than \$31 million in Title I- Set Aside carryover funds from previous years. Federal funds are available for 27 months after appropriation. If funds remain unexpended after this time period, they must revert to the federal government.

RECOMMENDATIONS: *Staff recommends* that the Subcommittee direct LAO to work with CDE and DOF to develop options for dealing with the additional program improvement districts in the current year and establish priorities for limited funding given different district needs (e.g. some districts were identified PI on the basis of participation rates only).

QUESTIONS:

1. *What are the program requirements and costs associated with identification of 150 new program improvement districts?*
2. *Does the Legislature need to reassess the provisions of AB 2066 (Steinberg/2004) as it relates to programs and expenditures for districts in program improvement?*
3. *What assurances can CDE provide that the state will not lose any unspent federal Title I –Set Aside funds in the 2005-06?*
4. *What is the Governor’s plan for spending Title I Set-Aside funds in the budget year, particularly as it relates to utilizing one-time carryover funds?*

OUTCOME: **No action.**

ISSUE 11: Williams Settlement Funding

DESCRIPTION: The Governor's budget proposes two augmentations in 2005-06 for low performing schools pursuant to the 2004 Williams lawsuit settlement, as reflected in legislation passed in 2004 to reflect that settlement. Specifically, the budget provides a \$45 million General Fund augmentation to fund a new cohort of the High Priority Schools program. In addition, the Governor appropriates \$100 million from the Proposition 98 Reversion Account for emergency facility repairs to schools in Deciles 1 to 3 on the Academic Performance Index (API).

BACKGROUND: The *Elizier Williams v. State of California* (Williams) lawsuit was a class action suit filed in Superior Court in 2000 on behalf of nearly 100 San Francisco student plaintiffs. The plaintiffs alleged that the State of California and state education agencies failed to provide public school students with access to qualified teachers, instructional materials and clean and safe school facilities. Agreements were reached by parties during August 2004. The notice of settlement was approved by the San Francisco Superior Court in December 2004.

Funding Required for Williams Settlement: The 2004-05 budget package included \$188 million in one-time funding specifically for the Williams settlement agreement, which was still underway in the final days of the budget. For this reason, agreements were further specified in a number of bills enacted at the 2004 session. Funds appropriated in 2004-05 for the Williams settlement include:

- \$138 million in one-time funding for instructional materials for students in Deciles 1 & 2 of the API.
- \$50 million in one-time funds that were "set-aside" (not appropriated) in the budget package for "other" Williams settlement costs. This \$50 million was later appropriated by SB 550. Funds were provided for the following purposes, as specified in both SB 550 and SB 6:
 - \$15 million for County Office of Education oversight of schools in Deciles 1, 2, and 3 of the API to assure for teacher misassignment, condition of school facilities, and adequacy of instructional materials.
 - \$5 million to the CDE for the purchase of textbooks. These funds are an advance as they will be repaid by districts.
 - \$ 5 million for Emergency School Repairs.
 - \$25 million for the School Facilities Needs Assessment Program.

In addition to funding included in the 2004-05 budget package, SB 6 and SB 550 contained two significant future funding requirements:

- SB 550 requires that new schools be added to the High Priority (HP) Schools program when current schools are phased out and that overall funding for the program is maintained at \$200 million annually.
- SB 6 requires that commencing with the 2005-06 Budget Act, and every year thereafter, the state transfer **\$100 million** or 50 percent of the funds appropriated from the Proposition 98 Reversion Account, *whichever is greater*, to the School Facilities Emergency Repair Account (SFERA). This program provides grants to school districts in Deciles 1-3 of the 2003 API. SB 6 requires that funds shall be transferred into the account until a total of \$800 million has been disbursed from the SFERA. SB 6 authorizes the Legislature to transfer other one-time funds to the SFERA.

The Governor's 2005-06 budget proposes two appropriations that are consistent with the Williams funding requirements contained in SB 6 and SB 550. These appropriations include:

- **\$45 million** in General Funds to fund a new cohort of the High Priority Schools Grant Program in 2005-06. This would bring total funding for the program to \$238.7 million in 2005-06. Department of Finance estimates that \$45 million will provide funding to 180 additional Decile 1 schools (assuming 400 students per school).
- **\$100 million** in funding from the Proposition 98 Reversion Account to fund emergency facility repairs in Decile 1-3 schools. Funds will be provided to the School Facilities Emergency Repair Account and allocated by the State Allocation Board. Current law requires \$100 million, or 50 percent of Proposition 98 reversion funds, whichever is greater. For this reason, this appropriation will increase at May Revise if Proposition 98 Reversion Account funds increase.

The Governor does not propose to continue any of the \$188 million in one-time funding appropriated for Williams settlement purposes in 2004-05. However, the Governor does propose to continue augmentations – even small increases -- for the Instructional Materials Block Grant and the Deferred Maintenance programs in 2004-05. These current year augmentations were *related* to the Williams settlement. These two programs are presented later in the agenda.

For the HP new cohort, the LAO suggests that the Legislature should not create a new HP cohort until it (1) reassesses the state's intervention strategy in low performing schools and districts, and (2) determines the funding mechanism and source of funds for HP schools that failed to make significant progress over the last three years.

RECOMMENDATION: *Staff recommends* approval, but notes that the appropriation for the School Facilities Emergency Repair Account could increase above \$100 million at May Revise if Proposition 98 reversion funds exceed budgeted levels.

OUTCOME: **No action.**

ISSUE 12: Instructional Materials

DESCRIPTION: The Governor proposes \$380.3 million in 2005-06 for the Instructional Materials Block Grant. This proposal continues funding at 2004-05 levels, adjusted for growth and COLA. The one-time set-aside of \$30 million for supplemental materials for English learners established in 2004-05 is eliminated, but funding is retained for ongoing instructional materials programs.

BACKGROUND: The Instructional Materials Block Grant program provides funding to school districts for the purchase of standards-aligned instructional materials for students in grades K-12. Funding is allocated to districts on the basis of enrolled students in grades K-12.

The 2004-05 budget includes \$363 million in ongoing funds for the Instructional Materials Block Grant, which represents an increase of \$188 million from the 2003-04 budget. This augmentation was related to the Williams lawsuit settlement. Of the \$188 million in additional funds, \$30 million was set-aside on a one-time basis for supplemental materials for English Learners.

The LAO does not take issue with the Governor's proposal.

RECOMMENDATION: *Staff recommends* approval as budgeted.

OUTCOME: **Approved as budgeted. (3-0)**

ISSUE 13: Deferred Maintenance

DESCRIPTION: The Governor's 2005-06 budget proposes \$267.4 million in ongoing funding for the Deferred Maintenance program, an augmentation of \$29.6 million in ongoing funding above 2004-05 levels. The Governor proposes this augmentation to fully fund the program at the level required in statute.

BACKGROUND: The state Deferred Maintenance program provides state and local funding for major repair or replacement of school facilities. The State Allocation Board allocates funds to applicant local school districts, which are required to fully match state dollars in order to participate in the program.

Deferred maintenance, which is different from routine maintenance, is defined as the repair or replacement work performed on a school facility that is not performed on an annual, ongoing basis, but is planned for the future and part of each district's five year plan. Typical projects include major maintenance and infrastructure projects such as exterior painting, roof replacement, and long-term repairs to electrical, heating, and plumbing systems.

Education Code 17584 requires the state to provide funding equal to 0.05 percent of district revenue limits and other funds for the Deferred Maintenance program. The Deferred Maintenance program is not subject to statutory growth and COLA adjustments.

The 2004-05 budget package included \$250 million in ongoing funding for Deferred Maintenance, which represented an increase of \$173 million over 2003-04 funding. This augmentation was related to the Williams lawsuit settlement. Of the \$250 million provided in 2004-05, approximately \$12 million was one-time funding and \$238 million was one-time funding.

The LAO recommends approval of the Governor's proposal.

RECOMMENDATION: *Staff recommends* approval as budgeted.

OUTCOME: **Approved as budgeted. (3-0)**

Appendix A.

First Interim Status Report, 2004-05

www.cde.ca.gov/fg/gi/ir/first04.05.asp

Appendix B.

Budget Control Section 12.40: Categorical Programs and Transfer Authority

Budget Act Sec. 12.40 Categorical Flexibility

\$ in thousands

			Proposed Limits	
			10% out	15% in
	2005-06			
6110-111-0001	\$515,196	home to school transportation	\$51,520	\$77,279
6110-119-0001	\$9,477	educational services for foster youth	\$948	\$1,422
6110-122-0001	\$5,562	specialized secondary programs	\$556	\$834
6110-124-0001	\$46,110	gifted & talented pupil program	\$4,611	\$6,917
6110-128-0001	\$585,176	economic impact aid	\$58,518	\$87,776
6110-151-0001	\$4,688	American Indian education	\$469	\$703
6110-167-0001	\$4,698	vocational education	\$470	\$705
6110-181-0001	\$16,038	education technology programs	\$1,604	\$2,406
6110-193-0001	\$29,580	staff development	\$2,958	\$4,437
6110-203-0001	\$85,018	child nutrition	\$8,502	\$12,753
6110-209-0001	\$43	teacher dismissal apportionments	\$4	\$6
6110-224-0001	<u>\$88,145</u>	year-round school grant program	\$8,815	\$13,222
	\$1,389,731			

Appendix C.

**Funds for State Formula – Allocated and Selected Student Aid Programs
U.S. Department of Education
California**

<http://www.ed.gov/about/overview/budget/statetables/06stbystate.pdf>